

Message Text

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ACTION EB-08

INFO OCT-01 ARA-06 ISO-00 ERDA-05 AID-05 CEA-01 CIAE-00
CIEP-01 COME-00 DODE-00 FEAE-00 FPC-01 H-01 INR-07
INT-05 L-03 NSAE-00 NSC-05 OMB-01 PM-04 USIA-06
OES-06 SP-02 SS-15 STR-04 TRSE-00 ACDA-07 PA-01 PRS-01
/096 W

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R 261540Z JAN 77

FM AMEMBASSY BRASILIA

TO SECSTATE WASHDC 9805

INFO AMCONSUL RIO DE JANEIRO

AMCONSUL SAO PAULO

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EO 11652 NA

TAGS EGEN ENRG BR

SUBJECT: PRELIMINARY ASSESSMENT OF BOG'S "RATIONALIZATION" PROGRAM

1. SUMMARY. PRESS AND PUBLIC REACTION TO THE JANUARY 17 ANNOUNCEMENT BY PRESIDENT GEISEL OF MEASURES TO CUT GASOLINE AND FUEL OIL CONSUMPTION HAS BEEN NEGATIVE ON BALANCE. THE NEED TO REDUCE THE PAYMENTS DEFICIT IS GENERALLY ACKNOWLEDGED, BUT THERE ARE FEARS ABOUT THE EFFECTS ON EMPLOYMENT AND INFLATION, AND INCREASED SKEPTICISM ABOUT THE BOG'S WHOLE APPROACH TO COMPLEX ECONOMIC PROBLEMS. A REDUCTION IN GASOLINE CONSUMPTION PROBABLY WILL BE ACHIEVED, BUT AT A HIGH COST IN REDUCED EMPLOYMENT AND CONSUMER DISSATISFACTION. END SUMMARY.

2. THE INITIAL REACTION TO THE GOB'S 15-POINT PLAN TO RATIONALIZE THE CONSUMPTION OF PETROLEUM DERIVATIVES HAS BEEN NEGATIVE ON BALANCE, PARTICULARLY NEGATIVE ABOUT THE 2-CRUZEIRO PER LITER DEPOSIT
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ON GASOLINE PURCHASES. STILL, SOME OBSERVERS HAD PREDICTED A MORE NEGATIVE REACTION THAN HAS OCCURRED. PREDICTABLY, MOST OFFICIAL SECTORS HAVE GENERALLY APPLAUDED THE PROGRAM; ECONOMIC MINISTERS DESCRIBE IT AS NON-INFLATIONARY, CERTAIN TO BE EFFECTIVE, AND NOT SO HARSH OR BUREAUCRATICALLY DIFFICULT TO ADMINISTER AS RATIONING. OPPOSITION LEADERS HAVE

ATTACKED THE PLAN AS "UNCONSTITUTIONAL," "ILLEGAL," AND "EXTORTIONIST." (AT LEAST SOME OPPOSITION LEADERS PREFER RATIONING, HOWEVER, WHICH MIGHT HAVE HAD A GREATER IMPACT ON THE CONSUMER THAN THE MEASURES ANNOUNCED.) EDITORIALS IN MAJOR NEWSPAPERS HAVE SEE-SAWED BACK AND FORTH, SOMETIMES PRAISING THE RATIONALIZATION PROGRAM FOR ITS "INGENUITY" AND SOMETIMES BITTERLY CRITICIZING THE "INGENUITY" AND SOMETIMES BITTERLY CRITICIZING THE "HYPROCRISY" OF THE MEASURES, PARTICULARLY THE GASOLINE DEPOSIT, AND CHARGING THAT THE MEASURES HAVE COME 3 YEARS TOO LATE. THERE IS PARTICULAR CRITICISM OF CERTAIN SPECIFIC EFFECTS OF THE PROGRAM (E.G., UNEMPLOYMENT GENERATED BY THE ONE-THIRD REDUCTION IN SERVICE STATION OPERATION HOURS).

3. BUSINESSMEN STRESS THE PROGRAM'S INFLATIONARY ASPECTS AND THE INEVITABLE BUREAUCRACY, AND THEY QUESTION WHETHER THE COSTS OF THE DEPOSIT SCHEMES FOR GASOLINE AND FUEL OIL ARE WORTH THE RELATIVELY SMALL FOREIGN EXCHANGE SAVINGS EXPECTED (\$120 MILLION A YEAR HAS BEEN ESTIMATED BY ONE SAO PAULO GROUP). ECONOMISTS OF ALL PERSUASIONS SEEM STRONGLY OPPOSED TO THE SCHEME. THE AIR FORCE AND NAVY MINISTERS REPORTEDLY EXPRESSED ADVERSE REACTIONS-- A RARE BREAK IN THE USUAL PATTERN OF AT LEAST OVERT MILITARY SUPPORT FOR THE REVOLUTION'S ECONOMIC POLICIES.

4. REACTING TO CRITICISM, PRESIDENT GEISEL CHARGED ON JANUARY 20 THAT THOSE OBJECTING TO THE PROGRAM WERE "DEFEATISTS, PESSIMISTS, NEGATIVISTS, AND LIMITED OFFICIAL USE

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THOSE WHO ARE ALWAYS ANTI." HE SAID SOMETHING HAD TO BE DONE, PREFERABLY SHORT OF RATIONING, AND HIS PROGRAM WAS THE "LEAST BAD" OF A SERIES OF UNSATISFYING CHOICES. FINANCE MINISTER SIMONSEN HAS BEEN QUOTED IN THE PRESS AS COMPLAINING THAT PRICE INCREASES IN THE PAST CAUSED LESS REACTION THAN IS BEING GENERATED NOW.

5. IN GENERAL, THE CRITICISM FOR MEDIA, INFORMED

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PUBLIC, AND SOME GOB OFFICIALS (THE LATTER MAINLY
IN PRIVATE) IS FOCUSED ON THE INFLATIONARY
IMPACT, THE ECONOMIC COSTS, AND QUALITY OF
ECONOMIC POLICYMAKING, INCLUDING THE SECRECY
WITH WHICH DECISIONS WERE MADE. FINANCE MINISTER
SIMONSEN HAS ARGUED THAT THE NET IMPACT OF THE
2-CRUZEIRO DEPOSIT IS, ON BALANCE, DEFLATIONARY.

WHETHER THE MEASURE WILL IN FACT
END UP BEING DEFLATIONARY ALSO DEPENDS IN PART
ON HOW THE FUNDS ARE USED (8.E., WHETHER STERILIZED
OR EXPENDED), AS WELL AS ON THE INDIRECT (SECOND-
ROUND AND SUBSEQUENT) EFFECTS RESULTING FROM
CHANGES IN RELATIVE PRICES OF COMMODITIES
TRADED IN THE ECONOMY. SOME OF THE 30 BILLION CRUZEIROS
EXPECTED TO BE COLLECTED IS ALREADY BEING EARMARKED
FOR PRIORITY SPENDING PROGRAMS SUCH AS THE ALCOHOL-SUBSTITUTION-
FOR-GASOLINE PROGRAM, AND FOR URBAN TRANSPORTATION.

6. COMMENT. OVERALL, THE GOB'S "RATIONALIZATION"

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PLAN IS A CUMBERSOME, AWKWARD ATTEMPT TO STEER A MIDDLE COURSE
BETWEEN OUTRIGHT RATIONING
AND EXCLUSIVE RELIANCE ON PRICE HIKES TO CONTRAOL
THE CONSUMPTION OF PETROLEUM DERIVATIVES, PARTICULARLY
GASOLINE, THE CONSUMPTION OF WHICH STABILIZED
IN 1976 AS A RESULT OF HIGHER PRICES. THE
NEW MEASURES HELP RAISE THE PRICE OF GASOLINE
WELL ABOVE ITS SOCIAL OPPORTUNITY COST AT ANY
REALISTIC EXCHANGE RATE. PREVIOUS EXPERIENCE WITH
PRICE RISES FOR PETROLEUM DERIVATIVES SUGGESTS

THAT THERE WILL BE AT LEAST A SHORT-TERM REDUCTION IN GASOLINE,
AND A DECLINE IN THE RATE OF INCREASE OF FUEL OIL CONSUMPTION AS
A RESULT OF IMPLEMENTATION OF THE COMPULSORY DEPOSIT. IF ENFORCED
VIGOROUSLY, THESE AND OTHER MEASURES
(RESTRICTION ON PARKING, ETC.) WILL FORCE AN
INCREASED DEMAND FOR THE SERVICES OF THE ALREADY OVERBURDENED PUBLIC
TRANSPORT SYSTEMS IN BRAZIL. HOW QUICKLY PUBLIC TRANSPORT CAN BE
EXPANDED IS UNCLEAR AT PRESENT; BUT GIVEN BRAZIL'S IMPORT ES-
RESTRICTIONS, MOST NEW TRANSPORT EQUIPMENT
WILL HAVE TO COME FROM DOMESTIC PRODUCERS, AND THIS
WILL INVOLVE SOME DELAYS. ALTHOUGH THE GOB
IS RIGHT IN SAYING THAT THE NEW MEASURES SHOULD LEAD TO GREATER
PUBLIC SENSITIVITY TO THE DIMENSIONS OF
BRAZIL'S ENERGY PROBLEMS, THE NATURE OF THE MEASURES
COULD CONTRIBUTE TO PUBLIC CYNICISM.
IT ALSO REMAINS TO BE SEEN WHETHER THE COMPULSORY DEPOSIT
PROGRAM FOR GASOLINE AND FUEL OIL WILL LIVE UP TO THE EXPECTA-
TIONS OF POLICYMAKERS.

7. THE NEW MEASURES, AS OPPOSED TO STRAIGHT PRICE INCREASES,
HAVE THE APPEARANCE OF A CERTAIN
AMOUNT OF SLYNES. FINANCE MINISTER SIMONSEN ARGUES THAT NOT
INCLUDING FIRST-ROUND DEPOSIT COSTS IN INFLATION INDICES, AND
THEREFORE NOT PICKING UP THIS IMPACT IN THE CALCULATION OF MONE-
TARY CORRECTION, WILL HELP HOLD DOWN INFLATION THAT IS CREATED
THROUGH THE APPLICATION OF
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MONETARY CORRECTION TO WAGES AND TO RETURNS PAID ON CORRECTED
FINANCIAL ASSETS. BUT THIS NECESSARILY IMPLIES THAT INFLATION
INDICES WILL UNDERSTATE REALITY NOT ONLY BECAUSE FIRST-ROUND
EFFECTS OF THE DEPOSIT ARE OMITTED, BUT ALSO BECAUSE MONETARY
CORRECTION ONE AGAIN IS BEING DEBASED IN THE SENSE THAT THE
CORRECTION DIVERGES FROM INFLATIONARY REALITY.
CRIMMINS

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Message Attributes

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